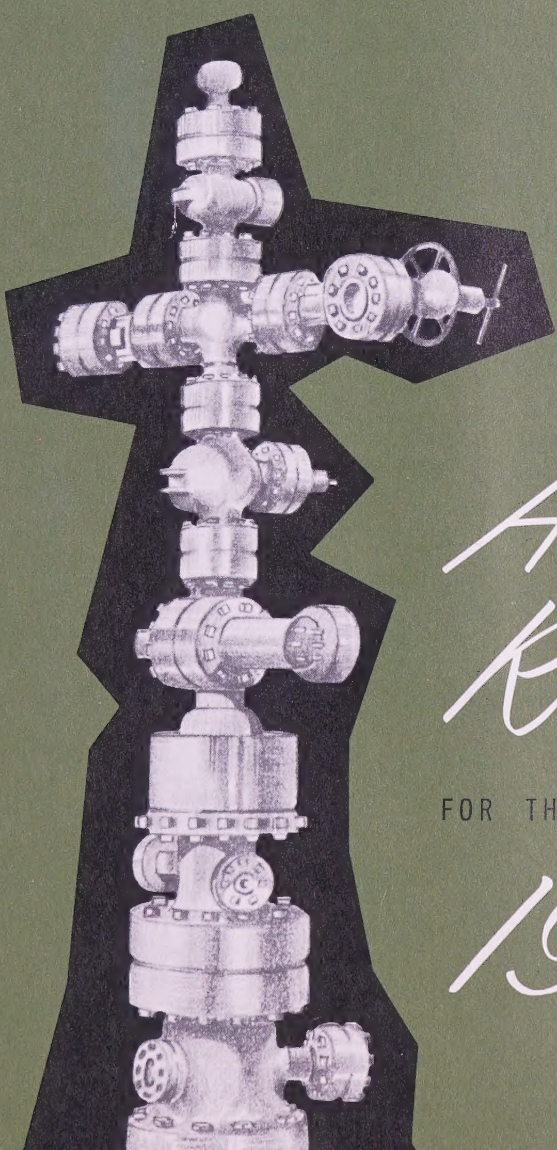
Hudson's Bay Oil and Gas Company Limited



Annual Report

FOR THE YEAR ENDED DECEMBER THIRTY-FIRST

1960

CONTENTS

Head Office

320 Seventh Avenue West, Calgary, Alberta, Canada

Transfer Agents and Registrars

Montreal Trust Company, Calgary, Toronto and Winnipeg
Morgan Guaranty Trust Company of New York, New York

Board of Directors

L. F. McCollum, Chairman, Houston, *President and a Director of Continental Oil Company*

Ira H. Cram, New York, *Chairman of the Executive Committee and a Director of Continental Oil Company*

M. J. Foley, Vancouver, *President and a Director of MacMillan, Bloedel and Powell River Limited*

Herbert H. Lank, Montreal, *President and a Director of Du Pont of Canada Limited*

J. R. Murray, Winnipeg, *Managing Director of Hudson's Bay Company*

G. T. Pearson, Calgary, *President of the Company*

Chas. A. Perlitz, Jr., Houston, *Executive Vice-President and a Director of Continental Oil Company*

L. J. Richards, Calgary, *Senior Vice-President of the Company*

James A. Richardson, Winnipeg, *Vice-President and a Director of James Richardson & Sons Limited and a Director of Hudson's Bay Company*

J. E. Woods, Winnipeg, *President and a Director of the Monarch Life Assurance Company and a Director of Hudson's Bay Company*

Officers

G. T. Pearson, President

L. J. Richards, Senior Vice-President

Howard W. Blauvelt, Senior Vice-President

K. H. Burgis, Financial Vice-President and Treasurer

D. C. Jones, Vice-President, Production

F. J. Mair, Controller

R. Suttill, Secretary

THE YEAR IN BRIEF

	1960	1959
FINANCIAL		
Gross Income	$22,409,000	$21,329,000
Net Income Before Special Credits		
Total	$ 1,004,000	$ 2,821,000
Per Share	$ .06	$ .16
Special Credits	$ 265,000	$ 943,000
Net Income for Year	$ 1,269,000	$ 3,764,000
Expenditures for Finding and Developing Reserves	$21,154,000	$17,849,000
OPERATING		
Crude Oil and Natural Gas Liquids Production — Net (Barrels Daily)	22,689	21,254
Natural Gas Sales — Net (Millions of Cubic Feet Daily)	44.309	44.957
Exploratory and Development Wells Completed		
Gross	140.0	185.0
Net	81.1	101.3
Net Acreage at December 31		
Fully or Partially Developed	164,000	135,000
Undeveloped	13,431,000	11,407,000
Total	13,595,000	11,542,000

REPORT TO THE SHAREHOLDERS

Operations — Net income, before special credits, of Hudson's Bay Oil and Gas Company Limited and subsidiary companies was $1,004,000 or 6 cents per share in 1960 compared with $2,821,000 or 16 cents per share in 1959. Special credits from sales of properties raised total net income to $1,269,000 in 1960.

The reduction of $1,817,000 in net income, before special credits, was primarily attributable to exploratory expenditures on large blocks of acreage in the Yukon-Northwest Territories and other virtually untested regions where geological conditions are favorable for large accumulations of crude oil and natural gas. The 1960 expenditures on these properties were substantially in excess of minimum outlays required by government regulations. Since this excess may be applied in reduction of subsequent obligations, only minor additional expenditures on these acreage blocks will be necessary in the next two years.

The Company's output of crude oil and natural gas liquids reached a new high in 1960. Net production averaged 22,689 barrels daily, an increase of 1,435 barrels daily or 6.8% over 1959. Development of the Virginia Hills and Garrington fields and a full year's production of natural gas liquids from the Windfall pilot cycling plant were major factors contributing to this increase.

Sales of natural gas at 44.3 million cubic feet per day, slightly less than in the prior year, continued to be restricted by inadequate market outlets. Although large scale exports of natural gas from Alberta to the United States were given final approval by governmental authorities last August, only limited deliveries to the new markets were made in 1960. Exports to the Midwest United States commenced last October but the principal new exports, those to the West Coast area of the United States, will not commence until late in 1961 after construction of the required transmission system has been completed. In 1960 the Company did not bring any of its major shut-in reserves of natural gas into production, but did start developing 11 natural gas properties.

Inclusive of both capital and expense items, expenditures for finding and developing reserves of crude oil and natural gas were $21,154,000. These expenditures were smaller than in the years 1955 and 1956, the peak period of development in the Pembina field, but larger than in any other year in the Company's history. The 1960 figure included $2,567,000 of capital and expense outlays for exploration in virtually untested areas where opportunities exist to enhance the Company's long-range reserve position.

Since the Company's inception in 1926 expenditures for finding, developing and producing reserves of hydrocarbons, together with administration costs and interest expense, totalled $213,600,000. In the same period sales of crude oil and natural gas and related revenues aggregated $131,900,000. Most of these expenditures and revenues are applicable to the period since the Leduc discovery in 1947. In this relatively short span of time 61.8% of gross expenditures have been recovered despite only nominal receipts from sales of natural gas and associated products. Although unrecovered expenditures were $81,700,000 at December 31, 1960, the Company had large reserves of crude oil, natural gas and associated products as well as extensive holdings of undeveloped acreage at that date.

In 1960 the value of the Company was again enhanced by a net addition to proved reserves of hydrocarbons. Discoveries, extensions and revisions of such reserves substantially exceeded production during the year.

Industry Affairs — By far the most important event in industry affairs in 1960 was the approval by governmental authorities of large scale exports of natural gas from Alberta to the United States. This action freed the industry to proceed with plans for the development of reserves and the construction of pipe line transmission systems required to implement deliveries of natural gas to waiting export markets. By October, 1960 deliveries had commenced under a permit to export up to 204 million cubic feet of natural gas per day to the Midwest United States. A pipe line now being constructed from Alberta to California will, upon completion, deliver up to 611 million cubic feet of natural gas per day to the San Francisco area and other markets en route.

The opening-up of new export markets will involve production of liquid hydrocarbons and sulphur as well as natural gas. The more important of these products is natural gas liquids

which will be produced in large volume. With the construction of supplementary gathering facilities, the liquids can be transported through the existing network of crude oil pipe lines for sale in widely dispersed domestic and foreign markets. Significant volumes of sulphur will also be produced as a by-product of the natural gas. The sulphur will have to compete for markets with other sources of production which at present are more than adequate to meet world demand.

In 1960 production of crude oil and natural gas liquids in Western Canada averaged 541,000 barrels per day, an increase of 21,000 barrels per day or 4% over the prior year but equivalent to only 49% of production capacity. Production for domestic use averaged 427,000 barrels per day, a decrease of 2,000 barrels per day from 1959. This decrease occurred despite a gain of 3% in total crude oil runs to Canadian refineries during the year. Foreign crude oil captured not only the entire growth in domestic demand but also a portion of the market previously supplied by crude oil from Western Canada. In 1960 Western Canada supplied only 57% of the crude oil required by Canadian refineries. Production for export markets averaged 114,000 barrels per day, an increase of 25% over the previous year. Crude oil exports to both the Puget Sound and Great Lakes areas of the United States increased substantially.

Outlook — The Company is now engaged in developing natural gas reserves which have been contracted for sale in export markets. The largest of the reserves under development is in the West Whitecourt block in Central Alberta from which sales are scheduled to commence early in 1962 through a new transmission system being constructed to serve the San Francisco market. In this block drilling of additional wells to meet delivery requirements and construction of gathering lines and processing facilities began late in 1960. The Company's share of the cost of this project is estimated at $11,256,000, of which only $610,000 had been spent to December 31, 1960.

The Company's sales of natural gas will increase materially when development of reserves dedicated to export markets has been completed. Deliveries from such reserves and scheduled increases in deliveries from reserves presently in production will raise the Company's natural gas sales to more than 100 million cubic feet per day. Production of associated liquids will increase to more than 5,500 barrels per day.

The prospects for an increase in the level of the Company's crude oil production now appear improved. The Canadian Government recently announced a national oil policy under which objectives for domestic production of crude oil and natural gas liquids were set at 640,000 barrels per day in 1961 and 800,000 barrels per day in 1963. The petroleum industry is being given an opportunity to achieve these production objectives by developing larger export markets and by voluntarily displacing foreign crude oil and refined products from the Ontario market so that the imposition of mandatory import controls will not be necessary.

The Company's capital expenditures are expected to be more than $20,000,000 in 1961 as compared with $17,283,000 in 1960. An increase of about $10,000,000 in expenditures to develop the West Whitecourt block will be partially offset by a reduction in other capital outlays. Part of the reduction will be accomplished by returning to a more normal level of activity in new exploratory regions such as the Yukon-Northwest Territories.

In May, 1960 Messrs. P. A. Chester and Joseph Harris retired from the Board of Directors. Mr. Chester had taken an active interest in the affairs of the Company since the late 1920's and had been a Director since 1941. Mr. Harris had been a Member of the Board since 1950. Through their wise counsel these men contributed immeasurably to the progress of the Company in a period of rapid growth and development. To fill the vacancies created by these retirements Mr. M. J. Foley, Vancouver, and Mr. J. R. Murray, Winnipeg, were appointed Directors. Mr. Foley is President of MacMillan, Bloedel and Powell River Limited and Mr. Murray is Managing Director of Hudson's Bay Company.

The Directors wish to record their appreciation for the imaginative and effective manner in which the Company's employees handled the many challenging problems faced during the year. Their efforts have established a sound base for future growth.

Additional operating and financial information is given in the general review which follows.

Submitted on behalf of the Board of Directors:

G. T. Pearson

President

Calgary, Alberta
March 7, 1961

Seismic operations in the North

GENERAL REVIEW

EXPLORATION

General — The Company's 1960 capital and operating expenditures for finding reserves of crude oil and natural gas, at $10,555,000, were greater than in any previous year. The increase in expenditures to a new peak was attributable to a sharp step-up in the program for evaluation of new exploratory regions. This program, which commenced in the Northwest Territories late in 1959, was intensified and extended into the Yukon and South Central British Columbia in 1960. However, the major portion of the Company's exploratory effort continued to be carried on in the established prospective areas of Alberta, Saskatchewan and Northeastern British Columbia.

Expenditures in the Yukon-Northwest Territories and South Central British Columbia to acquire additional acreage holdings and conduct a preliminary exploration program totalled $2,567,000. Geological and geophysical data secured by field parties and stratigraphic information obtained from drilling 4 gross or 1.7 net wells will be useful in selecting acreage to be retained and in planning future activities. Expenditures in these areas exceeded minimum requirements for the year imposed by government regulation, but the excess may be carried forward and is sufficient to satisfy most of the obligations for the next two years.

In the Athabasca tar sands in Northeastern Alberta, where the existence of large reserves of low gravity, bituminous crude oil has been established, a core hole drilling program was undertaken to appraise the quality of acreage holdings. The Company also participated in a pilot project to test the technical and commercial feasibility of in situ combustion as a method of up-grading and recovering these viscous crudes. Further work remains to be done to evaluate the commercial possibilities of this region.

Discoveries — Through its exploratory drilling program HBOG participated in 15 discoveries of new fields and extensions of existing fields in 1960. These discoveries and extensions are summarized in the table at the bottom of the page and those of most importance are discussed in the following paragraphs.

Near Fort Nelson, British Columbia, an exploratory well was completed in 359 feet of gas-bearing Devonian reef at a depth of 6,200 feet. This well, which extended the Clark Lake field 5 miles to the southwest, has a calculated open flow potential of 135 million cubic feet of natural gas per day. An extension well drilled early in 1961 two miles southwest of the previous completion encountered 327 feet of gas-bearing Devonian reef, confirming the importance of this natural gas reserve. The wells are located on a 231,700 acre permit in which a 30% interest is owned.

At Pocketknife, in the foothills area of Northeastern British Columbia, an exploratory well was completed in the Mississippian formation at a depth of 5,000 feet with a calculated open flow potential of 27 million cubic feet of natural gas per day. Additional drilling will be required to determine the importance of this natural gas reservoir which is in a complex geological structure. A 50% interest is owned in the well and in the 24,600 acre permit on which it was drilled. Three adjoining permits totalling 222,000 acres are 100% owned.

In the Milligan Creek area of Northeastern British Columbia significant reserves of crude oil have been found at relatively shallow depths in Triassic sands. The Milligan Creek field was discovered in 1957 and subsequent drilling has established the existence of an important crude oil reservoir. Early in 1960 the Wildmint exploratory well was completed 6½ miles southeast of the Milligan Creek field, testing 167 barrels of crude oil per day from a Triassic sand at a depth of 3,700 feet. The Woodrush exploratory well was then drilled 4 miles east of the Milligan Creek field, also finding crude oil in a Triassic sand. These discoveries are located on a 54,200 acre

DISCOVERIES AND EXTENSIONS IN 1960

Name of Field or Area (1)	Discoveries and Extensions: Number	Discoveries and Extensions: Nature	Producing Formation	Approximate Depth (feet)
Clark Lake	1	Natural Gas	Devonian	6,200
Pocketknife	1	Natural Gas	Mississippian	5,000
Wildmint	1	Crude Oil	Triassic	3,700
Woodrush	1	Crude Oil	Triassic	3,700
Caroline	1	Crude Oil	Cretaceous	7,200
Wintering Hills	2	Crude Oil	Cretaceous	4,500 - 4,700
Wintering Hills	2	Natural Gas	Cretaceous	3,300 - 4,400
Kaybob	2	Natural Gas	Cretaceous and Triassic	5,700 - 7,000
South Kaybob	1	Natural Gas	Cretaceous	7,300
North Lanaway	1	Crude Oil	Cretaceous	6,000
Three Hills Creek	1	Natural Gas	Mississippian	5,900
Schneider Lake	1	Natural Gas	Cretaceous	3,300

(1) The first 4 fields listed above are in Northeastern British Columbia; the other 8 fields are in Alberta.

block of leases and permits in which a 50% interest is owned. Although potential net production from this area is 1,500 barrels of crude oil per day, actual production has been insignificant due to the lack of a pipe line outlet. A permit to construct a pipe line connection from crude oil fields in Northeastern British Columbia to an existing carrier serving the Vancouver market was recently granted to Westcoast Transmission Company Limited by governmental authorities in British Columbia. Adequate market outlets at reasonable wellhead prices will provide the incentive for greatly increased exploratory and development activity in this region.

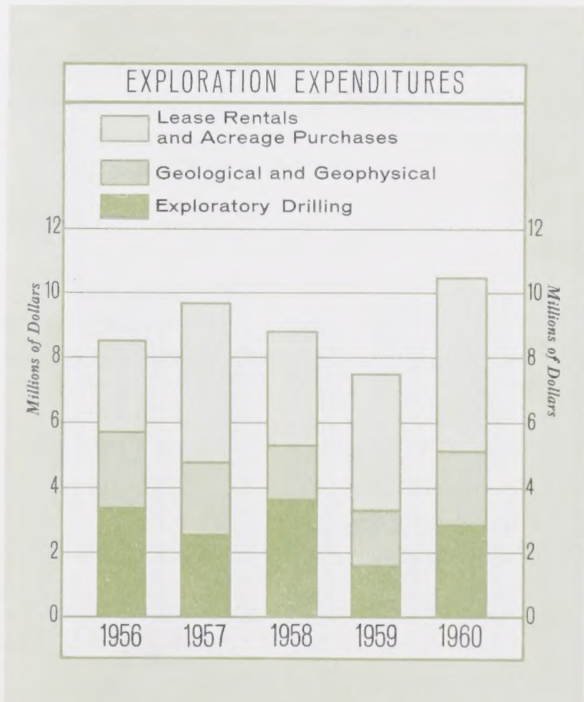
In the Caroline area of Central Alberta, 8 miles northwest of the Garrington crude oil field, an exploratory well was completed in a Cretaceous sand at a depth of 7,200 feet. This well, located on a lease block in which the Company owns 5,680 net acres, has a production potential of 242 barrels of crude oil per day. Development drilling is in progress on this block.

In the Wintering Hills area of Southeastern Alberta exploratory work was continued on a 170,000 acre block of leases in which interests varying from 33⅓% to 50% are owned. In 1960 four exploratory wells, all completed in Cretaceous sands at depths of 4,700 feet or less, resulted in 2 crude oil and 2 natural gas discoveries. In prior years 8 Cretaceous wells were successfully completed in this block, 4 as crude oil discoveries and 4 as natural gas discoveries. Although the reservoirs are not believed to be extensive, this area is attractive for further exploration and development because of the low cost of drilling to the shallow producing horizons, the high success ratio experienced, and the proximity of both crude oil and natural gas pipe line connections.

Acreage Holdings — The Company continues to acquire and process acreage in most of the prospective areas of Saskatchewan, Alberta and Northeastern British Columbia. In addition, substantial land holdings have recently been acquired in such new areas as the Yukon-Northwest Territories and South Central British Columbia where geological conditions are favorable for oil and gas accumulations. At December 31, 1960 holdings of undeveloped lands in Western Canada aggregated 13,431,400 net acres. The investment in undeveloped lands at that date was $9,646,000 or an average cost of 72 cents per acre. Applicable rentals paid in 1960 were $2,169,000 or an average of 16 cents per acre.

During the year 3,414,300 net acres of undeveloped lands were acquired. The major additions were 1,302,000 net acres in the Williams Lake area of South Central British Columbia, 1,276,100 net acres in the Yukon, 219,100 net acres in the Camsell Bend area of the Northwest Territories, 200,000 net acres in the Battleford area of Central Saskatchewan and 97,400 net acres in the Royce area of Northwestern Alberta.

In the same period 1,363,200 net acres of undeveloped lands were relinquished and 26,700 net acres were transferred to the producing category. Of the surrenders, 1,233,200 net acres were released for geological reasons, including



437,000 net acres in the Yukon. An additional 109,500 net acres were surrendered in accordance with provincial regulations upon conversion of reservations and permits to petroleum and natural gas leases. Contributions of 20,500 net acres were made to others in exchange for the drilling of exploratory wells on or adjacent to the Company's lands. Such contributions are a means of using the Company's strong acreage position in lieu of cash in carrying out its exploration program.

Undeveloped acreage holdings at December 31, 1960 are tabulated at the bottom of the page.

DRILLING

During the year the Company and its partners completed a total of 140 wells, 44 exploratory wells and 96 development wells. An additional 10 exploratory wells drilled on locations adjacent to HBOG's properties were supported with relatively small contributions of cash or acreage. Altogether, the Company participated in or supported 150 wells, 54 exploratory wells and 96 development wells.

The Company's interest in exploratory completions was equivalent to 21.3 net wells. Payment in cash was made for 15.0 of these net wells and acreage interests were assigned to obtain the drilling of the remaining 6.3 net wells. Successful exploratory completions were 3.0 net oil wells and 4.0 net gas wells.

Development completions were equivalent to 59.8 net wells. Successful completions were 47.9 net oil wells and 7.1 net gas wells. The distribution by fields of net development wells completed as crude oil producers was: Pembina 12.3; Virginia Hills 12.2; Garrington 5.5; Weyburn 5.0; Steelman 4.8; Pinto 3.0, and other fields 5.1. The distribution by fields of net development wells completed as natural gas producers was: Kessler 3.2; Pine Creek 1.7, and other fields 2.2.

Fewer wells were completed in 1960 than in the prior year. The decreases were 7 exploratory wells supported with contributions of cash or acreage, 8 gross or 5.6 net exploratory wells in which participating interests were owned, and 37 gross or 14.6 net development wells. This was a decrease of 19.9% in the number of net exploratory and development wells completed but, with an increase in average depth, the applicable footage drilled declined only 8.1%.

The cost of unsuccessful wells and abandonments charged to operations was $3,131,000, an increase of $921,000 over 1959. This increase was caused by drilling a greater number of deep exploratory wells in previously untested areas.

UNDEVELOPED ACREAGE HOLDINGS

December 31, 1960

Location	Crown Permits or Reservations (1)	Options To Lease: Hudson's Bay Company Lands	Options To Lease: Other Lands	Leaseholds	Total
Alberta	530,600	1,461,100	18,000	1,976,300	3,986,000
British Columbia	4,087,700	6,100	—	8,400	4,102,200
Saskatchewan	202,700	2,335,400	—	89,700	2,627,800
Yukon-Northwest Territories	2,011,700	400	—	—	2,012,100
Other	—	698,900	—	4,400	703,300
	6,832,700	4,501,900	18,000	2,078,800	13,431,400

(1) Convertible into leases to the extent of approximately 50%

PRODUCTION

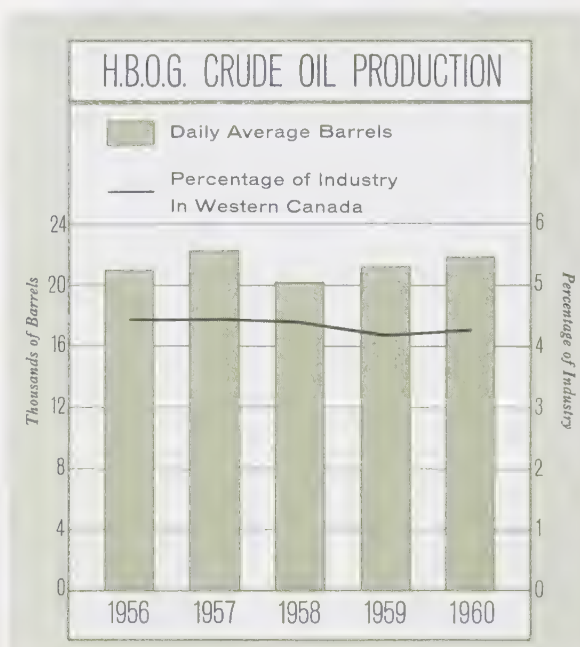
Crude Oil — Net crude oil production averaged 21,929 barrels daily, slightly below the peak attained in 1957 but up 882 barrels daily or 4.2% over 1959. Production from new wells completed in 1960 and a full year's operation of wells completed in the prior year contributed 2,373 barrels daily to the total production figure. Reductions in well allowables of 1,053 barrels daily and natural decline in production from older wells of 438 barrels daily partly offset this increase.

Production by fields, with comparative figures for 1959, is shown below.

	Net Production (Daily Average Barrels)	
	1960	1959
Pembina	7,527	7,730
Sundre	2,075	2,041
Sturgeon Lake South	1,208	1,400
Leduc-Woodbend	942	1,034
Garrington	819	358
West Drumheller	765	939
Success	735	762
Cessford	603	487
Innisfail	556	403
Fenn-Big Valley	549	653
Virginia Hills	425	52
Other Fields	5,725	5,188
Total	21,929	21,047

During the year increases in the capacity to produce crude oil in Western Canada continued to outpace the growth in market demand. Since 1957, production of crude oil in Western Canada has increased only 4% while production capacity has gone up 20%. The resulting imbalance in supply-demand relationships has exerted almost continuous downward pressure on crude oil prices as evidenced by aggregate decreases of 11% since 1957. This imbalance also exerted upward pressure on costs of operation. With the number of wells capable of producing crude oil rising more rapidly than market demand, rates of production per well have steadily declined, causing increases in unit production costs.

To counteract the effects of the cost-price squeeze the Company has continued to focus attention on improving efficiency of operations. As one method of accomplishing this objective, 30 agreements for unitizing operations have been completed and 12 additional unitization agreements are being negotiated. Under unitization arrangements ownership of field facilities and future production with respect to individual properties is exchanged for an interest in the aggregate field facilities and future production with respect to all of the properties comprising the unit. Unitization permits designation of one operator for the combined properties and operation of the minimum number of wells required to achieve the unit's allowable production, with consequent savings in expenses and investments in wells, tank batteries and other facilities. By establishing uniform ownership interests over an extensive area, unitization also facilitates the installation of pressure maintenance systems.



The Company has continued to expand its participation in pressure maintenance projects designed to increase current rates of production and ultimate recoveries of crude oil. During 1960 projects affecting HBOG's properties were instituted or expanded in the Pembina, Harmattan-Elkton, Leduc and Turner Valley fields in Alberta and in the Instow and Bone Creek fields in Saskatchewan. The most extensive facilities have been installed in the Pembina field where, by year-end, 19,352 net acres had been put under pressure maintenance at a capital cost to the Company of $7,500,000.

In 1960 the Company's first full-scale automation system was put into operation in the Virginia Hills oil field. This system provides for programming of production, transfer of custody of crude oil from tank batteries to connecting pipe lines, running production tests on individual wells and location of mechanical failures, all automatically. Automation minimizes labor costs and prevents losses of production during severe weather.

Automation equipment - Virginia Hills

Natural Gas and Associated Products — Natural gas sales averaged 44.3 million cubic feet daily in 1960, slightly below the level of the prior year. Sales by fields, with comparative figures for 1959, are shown as follows:

Natural Gas Sales — Net
(Millions of Cubic Feet Daily)

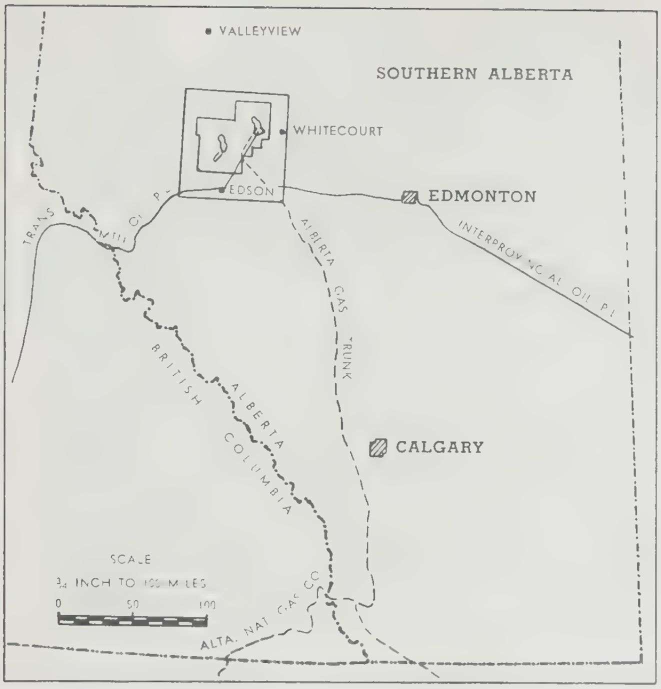
	1960	1959
Cessford	28.0	27.2
Pembina	7.4	8.4
Provost	1.6	1.8
Other Fields	7.3	7.6
Total	44.3	45.0

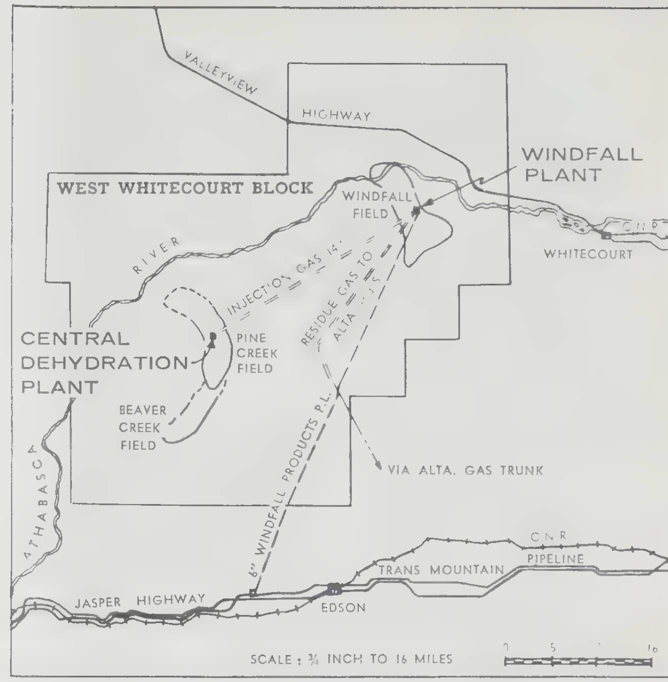
Net production of natural gas liquids averaged 760 barrels daily, an increase of 553 barrels daily over 1959. This increase was mainly due to a full year's operation of the Windfall pilot cycling plant which was brought into production in mid-1959.

During 1960 governmental authorities approved large-scale exports of natural gas from Alberta to the Midwest and West Coast areas of the United States. This action was the signal to the petroleum and natural gas industry to set in motion a program for construction of large diameter transmission systems, laying of gathering lines, construction of processing plants and drilling of additional wells to meet delivery requirements.

The Company, too, has started developing natural gas reserves dedicated to the new export markets. The largest of these reserves is in the West Whitecourt block in Central Alberta where facilities are being constructed to permit integrated operation of the Windfall, Pine Creek and Beaver Creek gas fields. The estimated cost to the Company of these facilities is $11,256,000.

Under the plan of operation for the West Whitecourt block, natural gas with high liquid but relatively low hydrogen sulphide content will be produced and delivered from the Windfall field to a plant which is now under construction. At the plant raw gas from the Windfall field will be processed to produce dry saleable gas, natural gas liquids and elemental sulphur. To prevent loss of recoverable liquids by condensation in the Wind-





fall reservoir, Pine Creek gas with high hydrogen sulphide but low liquid content will be delivered through a new 27 mile transmission line for injection into the Windfall reservoir. After the dry gas from the Pine Creek field has swept the condensate-rich gas from the Windfall reservoir, all three gas fields in the West Whitecourt block will be operated simultaneously to produce saleable gas and elemental sulphur.

The Company's net interest in daily production from the West Whitecourt project, when it goes on stream early in 1962, is estimated at 39.0 million cubic feet of natural gas, 5,300 barrels of natural gas liquids and 200 long tons of sulphur. Natural gas production will be delivered to Alberta and Southern Gas Co. Ltd. at the plant gate under a firm sales contract providing for prices per thousand cubic feet of 14½ cents until mid-1962, increasing to 16¼ cents during the next two years and gradually escalating thereafter to a maximum of 21 cents in 1983. Natural gas liquids are not normally sold under long-term contractual arrangements but it is expected that the Company's production will be readily saleable at satisfactory prices relative to crude oil. Further work remains to be done on arrangements for the disposition of sulphur but the economic success of the West Whitecourt project is not dependent on sales of this product.

In addition to the West Whitecourt project the Company is participating in the construction of gathering systems and plants in 10 other natural gas fields. Completion of these projects in 1961 and 1962 will result in further significant increases in net production of natural gas, associated liquids and sulphur.

PIPE LINES

During 1960 the Company's Rangeland Pipe Line Division, which comprises 192 miles of gathering and trunk lines in Central Alberta, transported an average of 23,597 barrels of crude oil per day, an increase of 6.9% over the prior year. This increase resulted primarily from the installation of additional gathering facilities in the Garrington, Gilby and Medicine River fields and from receipt through a connecting carrier of a greater portion of production from the Westward Ho and Harmattan-Elkton fields. Capital outlays for the installation of additional gathering facilities totalled $242,000 in 1960, bringing gross investment in the system to $6,564,000 at year end.

The Company operates and has a 41⅔% interest in a 46 mile pipe line from the Windfall pilot cycling plant to the Edson Station of the Trans Mountain Oil Pipe Line system. This connection permits natural gas liquids produced at the Windfall plant to be transported to markets

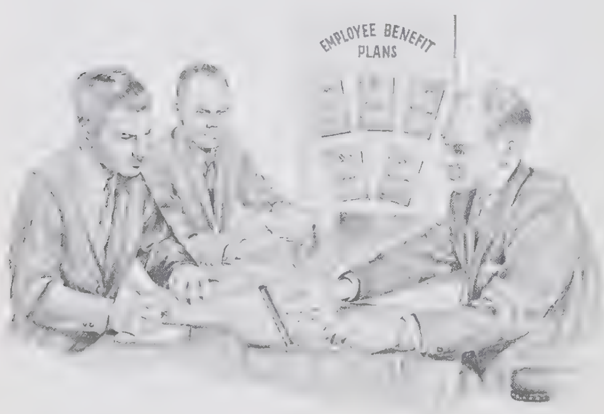
on the West Coast. Traffic through the Windfall line in 1960, the first full year of operation, averaged 1,617 barrels of natural gas liquids daily.

It is the Company's policy to encourage the construction and participate in the ownership of pipe lines in areas where it has major interests in reserves of crude oil or natural gas liquids. An 11% equity interest is owned in the Peace River Oil Pipe Line system which connects fields in the Sturgeon Lake area with Trans Mountain Oil Pipe Line. A 4% equity interest is owned in the Producers-Westspur system which gathers crude oil in Southeastern Saskatchewan and Southwestern Manitoba for delivery to Interprovincial Pipe Line. During the past year the Company took an active part in the formulation of plans to construct additional gathering lines in Alberta to handle the large volume of liquids which will be produced upon commencement of natural gas exports to the West Coast area of the United States.

EMPLOYEES

The cost-price squeeze experienced during 1960 caused increased emphasis to be placed on more effective use of manpower. Despite an increase in all phases of activity, staff was reduced by 5 employees during the year to a total of 407 at year end.

Salaries and wages paid in 1960, exclusive of benefits, totalled $2,395,000. The Company's contributions to benefit plans were $402,000 or 16.8% of salaries and wages, raising total manpower costs to $2,797,000. This was an increase of $115,000 over the comparable figure for the previous year. The major portion of the rise was due to a 4% general increase in salaries and wages granted April 1, 1960.



Explanation of Employee Benefit Plans

Two established benefit plans were completely revised and one new plan was made available to employees effective January 1, 1960. The Comprehensive Medical Expense Plan and the Group Life Insurance Plan were revised to provide broader coverage at reduced cost both to employees and the Company. A Supplemental Salary Continuance Plan, fully paid for by employees, was introduced to provide members with low-cost indemnity against loss of salaries during extended periods of disability. Acceptance of these plans has been excellent, with participation by eligible employees increasing from 80% to 98% in the medical plan and from 71% to 82% in the group life insurance plan. The new salary continuance plan has been subscribed to by 82% of eligible employees.

The Retirement and Thrift Plans were continued in effect without change. During the year the Company contributed $103,400 to the Retirement Plan and employees deposited $82,700, with 84% of those eligible participating. At year end the Thrift Plan trustee held, on behalf of members, assets with a total cost value of $216,100. In accordance with directions received from employees 84% of this amount had been invested in the Company's capital stock, with 14,021 shares being held at December 31, 1960. At that date 83% of eligible employees were participating in the Thrift Plan.

The Company's safety record was maintained at a high level in 1960. Employees achieved the lowest personal injury frequency and severity rates since 1951. These rates were also among the lowest for the petroleum industry in Western Canada.

FINANCIAL

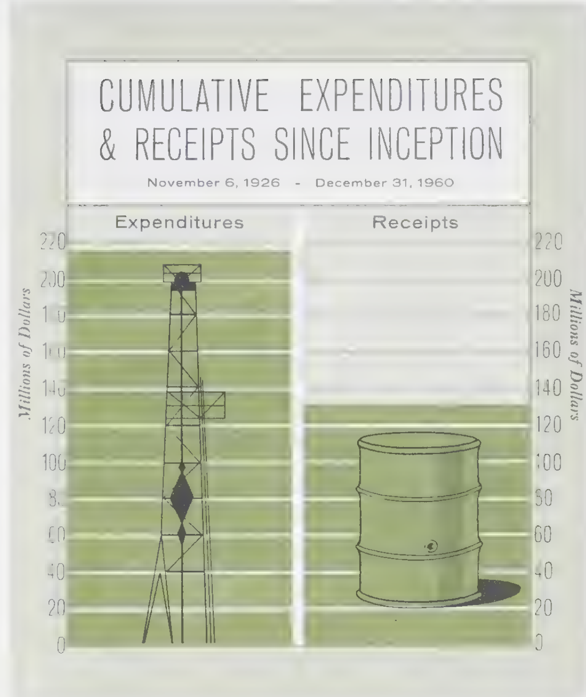
Net income in 1960, exclusive of special credits, was $1,004,000 or 6 cents per share, a reduction of $1,817,000 or 10 cents per share from the comparable net income in 1959. This reduction in earnings was more than accounted for by an increase in exploration expenses. Profits realized from sales of properties brought total net income for 1960 to $1,269,000.

Gross operating income was $22,021,000, an increase of $1,047,000 or 5.0% over the previous year. The sources of this gross operating income, together with increases over the prior year, are shown in the following table.

	Gross Operating Income	
	Amount In 1960	Increase Over 1959
Sales of crude oil	$17,720,000	$ 369,000
Sales of natural gas liquids	588,000	512,000
Sales of natural gas and revenues from related operations	1,872,000	46,000
Revenues from pipe line and related operations	1,841,000	120,000
Total	$22,021,000	$1,047,000

The gain in crude oil sales reflected the net effect of an increase of 4.3% in volumes sold and a reduction of 2.1% in average prices received. The increase in sales of natural gas liquids resulted primarily from a full year's operation of the Windfall pilot cycling plant.

Total expenses were $21,405,000, an increase of $2,897,000 or 15.7% over 1959. Expansion of the Company's exploration program caused an increase in expenses of $2,056,000, of which $1,637,000 represented the expensed portion of outlays in the Yukon-Northwest Territories, South Central British Columbia and the Athabasca tar sands. Expenses of producing operations increased $502,000 in 1960. This increase was primarily attributable to continued growth in the number of wells on production, expansion of pressure maintenance programs and



Finding, developing and producing costs plus administration and interest charges; receipts from oil and gas sales; since inception in 1926 but mainly applicable to the period since the Leduc discovery in 1947.

enlargement of natural gas plant operations. Pipe line expenses were up $203,000, largely as the result of a change from a straight-line to a unit-of-throughput method of calculating depreciation.

No provision for income taxes was required in 1960. As explained in Note 4 to the financial statements, the Company has accumulated substantial deductions which it is permitted to carry forward to offset taxable income of future years.

The Company's expenditures for property, plant and equipment totalled $17,283,000, up $2,604,000 over 1959. Outlays to drill and equip exploratory and development wells increased $1,544,000 and acreage acquisitions increased $1,047,000. The 1960 expenditures included $610,000 of preliminary costs incurred prior to the year end on an $11,256,000 project to bring the West Whitecourt natural gas reserves into full production by early 1962.

As shown in the following statement of Sources and Uses of Funds, net cash flow from operations was $11,064,000 or 62 cents per share, virtually the same as in the previous year.

SOURCES AND USES OF FUNDS

	1960	1959
Sources of Funds:		
Net income before special credits	$ 1,004,000	$ 2,821,000
Non-cash charges for depletion, depreciation, dry holes, surrendered leases and amortization of debt expense	10,060,000	8,260,000
Cash generated from operations	11,064,000	11,081,000
Sales of properties	1,057,000	5,477,000
Total funds available	$12,121,000	$16,558,000
Uses of Funds:		
Expenditures for property, plant and equipment	$17,283,000	$14,679,000
Reduction of long-term debt	100,000	1,100,000
Miscellaneous uses (sources) of funds	234,000	(34,000)
Total funds used	$17,617,000	$15,745,000
Resulting Increase (Decrease):		
In cash and short-term securities	$(5,015,000)	$ 386,000
In other working capital items	(481,000)	427,000
In total working capital	$(5,496,000)	$ 813,000

The consolidated financial statements include the accounts of Rangeland Pipe Line Company Limited and Hub Air Ltd. These companies are being maintained in an inactive status and, accordingly, had only nominal operations in 1960.

Hudson's Bay Oil and Gas Company Limited

and Subsidiary Companies

CONSOLIDATED STATEMENT OF INCOME

YEARS ENDED DECEMBER 31, 1960 AND 1959

	1960	1959
INCOME:		
Gross operating income	$22,021,000	$20,974,000
Interest, dividends and other income	388,000	355,000
	22,409,000	21,329,000
EXPENSES (Note 1):		
Operating and general expenses (Note 2)	7,684,000	6,343,000
Rentals of undeveloped oil and gas properties	2,169,000	2,346,000
Taxes, other than income taxes	467,000	426,000
Dry holes and abandonments	3,131,000	2,210,000
Surrendered leases	290,000	135,000
Depletion	3,943,000	3,675,000
Depreciation (Note 3)	2,561,000	2,188,000
Interest and expense on long-term debt	1,160,000	1,185,000
	21,405,000	18,508,000
NET INCOME BEFORE SPECIAL CREDITS	1,004,000	2,821,000
SPECIAL CREDITS, principally from sales of properties	265,000	943,000
NET INCOME FOR YEAR (Note 4)	$ 1,269,000	$ 3,764,000

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

YEARS ENDED DECEMBER 31, 1960 AND 1959

	1960	1959
Balance at Beginning of Year	$ 8,181,000	$ 4,417,000
Net Income for Year	1,269,000	3,764,000
Balance at End of Year	$ 9,450,000	$ 8,181,000

ASSETS

	1960	1959
CURRENT ASSETS:		
Cash	$ 883,000	$ 608,000
Government and other securities at cost, which approximates market	4,751,000	10,041,000
Accounts receivable	5,301,000	5,351,000
Inventories of crude oil and supplies at or below average cost	1,630,000	1,826,000
Total Current Assets	12,565,000	17,826,000
INVESTMENTS IN NON-CONTROLLED COMPANIES AT COST	477,000	474,000
PROPERTY, PLANT AND EQUIPMENT AT COST	117,915,000	105,809,000
LESS: Accumulated depreciation and depletion	31,878,000	26,338,000
	86,037,000	79,471,000
OIL AND GAS RIGHTS ON HUDSON'S BAY COMPANY LANDS	1,000	1,000
OTHER ASSETS:		
Unamortized bond discount	438,000	481,000
Operating and performance deposits	636,000	360,000
Miscellaneous	242,000	287,000
	1,316,000	1,128,000
	$100,396,000	$ 98,900,000

Approved on Behalf of the Board:

G. T. Pearson, DIRECTOR

L. J. Richards, DIRECTOR

LIABILITIES AND SHAREHOLDERS' EQUITY

	1960	1959
Current Liabilities:		
Accounts payable and accrued liabilities	$ 4,442,000	$ 4,206,000
Long-term debt due within one year	100,000	100,000
Accrued bond interest	226,000	227,000
Total Current Liabilities	4,768,000	4,533,000
Long-Term Debt (Note 5):		
First Mortgage Sinking Fund Bonds: 4% Series A, maturing May 1, 1975	23,000,000	23,000,000
5% Series B, maturing October 1, 1971, exclusive of amounts due within one year	900,000	1,000,000
5¾% Series C, maturing August 1, 1977	2,500,000	2,500,000
	26,400,000	26,500,000
Deferred Credit re Office Building (Note 6)	904,000	812,000
Shareholders' Equity:		
Share capital, par value $2.50 per share: Authorized: 25,000,000 shares; Issued and outstanding: 17,744,592 shares	44,362,000	44,362,000
Paid-in surplus	14,512,000	14,512,000
Retained earnings	9,450,000	8,181,000
	68,324,000	67,055,000
	$100,396,000	$ 98,900,000

Commitments — See Note 7

Note 1: The Company's accounting practice is to charge exploration expenses against income as incurred. The cost of drilling successful wells is capitalized and amortized on a unit of production basis, and the cost of unsuccessful wells is expensed upon completion.

Note 2: The following amounts were paid during the year ended December 31, 1960: Directors' fees and expenses $24,000; salaries of executive officers $179,000; fees and salaries for legal counsel $35,000.

Note 3: Effective January 1, 1960 the method of providing for depreciation of certain pipe line assets was changed from a straight-line to a unit-of-throughput basis. The provision for depreciation of pipe line assets was $509,000 in 1960, an increase of $131,000 over the amount which would have been provided if the straight-line method had been continued in use.

Note 4: Under the provisions of the Income Tax Act and Regulations, oil companies are permitted to deduct currently exploration expenses and the costs of drilling both successful and unsuccessful wells and also are allowed, in general, to carry forward any excess of such deductions over income. As a result of these provisions, no income tax was payable in respect of 1960 operations, and the Company had a substantial carry-forward at December 31, 1960 to apply against taxable income of future years.

Note 5: The First Mortgage Sinking Fund Bonds are secured under a Deed of Trust and Mortgage by a first fixed and specific mortgage and charge on certain petroleum and natural gas leases and by a first floating charge on all other property and assets of the Company, both present and future. Under the provisions of the Deed of Trust and Mortgage, payments sufficient to redeem the following principal amounts of bonds are required: 4% Series A bonds — $1,000,000 in each of the years 1961 to 1974, inclusive, with the balance of $10,000,000 payable in 1975; 5% Series B bonds — $100,000 in each of the years 1961 to 1969, inclusive, with the balance of $100,000 payable in 1970 and 1971; 5¾% Series C bonds — $160,000 in each of the years 1962 to 1976, inclusive, with the balance of $100,000 payable in 1977. As a result of the purchase and surrender to the Trustee of Series A bonds, the Company had a sinking fund credit at December 31, 1960 of $1,000,000 which may, at its option, be applied against any of the future sinking fund payments required for these bonds. Subject to certain restrictions and conditions, the Company may issue additional bonds secured by the Deed of Trust and Mortgage.

Note 6: On December 1, 1959 the Company sold its Calgary office building and simultaneously entered into a long-term lease for the property at annual net rentals of 3½% of the selling price for a minimum period of 5 years and at higher rates thereafter. Under the terms of the lease, the Company has an option, for a minimum period of 5 years from the date of sale, to repurchase the property at the original selling price and to cancel the lease. The excess of the selling price over the depreciated value of the property at the date of sale and a charge in lieu of depreciation since that date have been recorded in the accounts as a deferred credit. The balance in this account will be credited to accumulated depreciation if the building is repurchased and otherwise will be credited against future rentals.

Note 7: The Company has contracted for the sale of natural gas from the West Whitecourt area with deliveries to commence early in 1962 at a net rate of 39.0 million cubic feet daily. To provide for these deliveries of natural gas, as well as the production of associated liquids and sulphur, a program to drill additional wells and construct gathering and processing facilities has been undertaken. The cost to the Company of this program is estimated at $11,256,000, of which $10,646,000 remains to be spent.

PEAT, MARWICK, MITCHELL & CO.

CHARTERED ACCOUNTANTS

ROOM 508
309 EIGHTH AVENUE WEST
CALGARY, ALBERTA

AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the consolidated balance sheet of Hudson's Bay Oil and Gas Company Limited and subsidiary companies as of December 31, 1960 and the consolidated statements of income and retained earnings for the year ended on that date and have obtained all the information and explanations we have required. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion (according to the best of our information and the explanations given to us and as shown by the books of the companies) the accompanying consolidated balance sheet and consolidated statements of income and retained earnings are properly drawn up so as to exhibit a true and correct view of the state of the affairs of Hudson's Bay Oil and Gas Company Limited and subsidiary companies at December 31, 1960 and the results of their operations for the year ended on that date, in accordance with generally accepted accounting principles which, except for the change (of which we approve) in the method of providing for depreciation of certain pipe line assets as set forth in Note 3 to the financial statements, have been applied on a basis consistent with that of the preceding year.

Peat, Marwick, Mitchell & Co.

Calgary, Alberta
February 11, 1961

Chartered Accountants

TEN YEAR FINANCIAL AN

		1960	1959
Income — *Financial Data*	Gross operating income	$ 22,021	20,974
	Net income (loss) before special credits:		
	Total	$ 1,004	2,821
	Per Share	$ .06	.16
	Special credits	$ 265	943
	Net income (loss) for year	$ 1,269	3,764
	Working capital	$ 7,797	13,293
	Current ratio	2.6	3.9
	Long-term debt	$ 26,400	26,500
	Shareholders' equity	$ 68,324	67,055
Gross Property Accounts	Leases	$ 17,659	14,605
	Wells, plants and equipment	$ 92,548	83,701
	Pipe line property	$ 6,564	6,334
	Other	$ 1,144	1,169
	Total	$117,915	105,809
Expenditures For Finding And Developing Reserves (2)	Acreage acquisitions	$ 3,344	2,297
	Exploratory expenses	$ 2,251	1,678
	Lease rentals	$ 2,169	2,346
	Drilling costs	$ 6,683	5,867
	Plants and equipment	$ 6,707	5,661
	Total	$ 21,154	17,849
Crude Oil And Natural Gas Liquids Production - Net	Average barrels daily	22,689	21,254
	Alberta	20,285	19,168
	Saskatchewan	2,386	2,026
	Other provinces	18	60
	Annual barrels (thousands)	8,304	7,758
Natural Gas Sales - Net (3)	Millions of cubic feet daily	44.309	44.957
	Billions of cubic feet annually	16.217	16.409
Wells	Completed		
	Gross wells	140.0	185.0
	Net wells	81.1	101.3
	Net development wells	59.8	74.4
	Oil wells	47.9	62.9
	Gas wells	7.1	6.4
	Dry holes	4.8	5.1
	Net exploratory wells	21.3	26.9
	Oil wells	3.0	3.5
	Gas wells	4.0	1.5
	Dry holes	14.3	21.9
	Capable of production		
	Total wells	726.6	677.0
	Oil wells	646.6	605.8
	Gas wells	80.0	71.2
Net Acreage	Thousands of acres	13,595	11,542
	Fully or partially developed	164	135
	Undeveloped	13,431	11,407
	Number of shareholders	11,956	12,171
	Number of employees	407	412

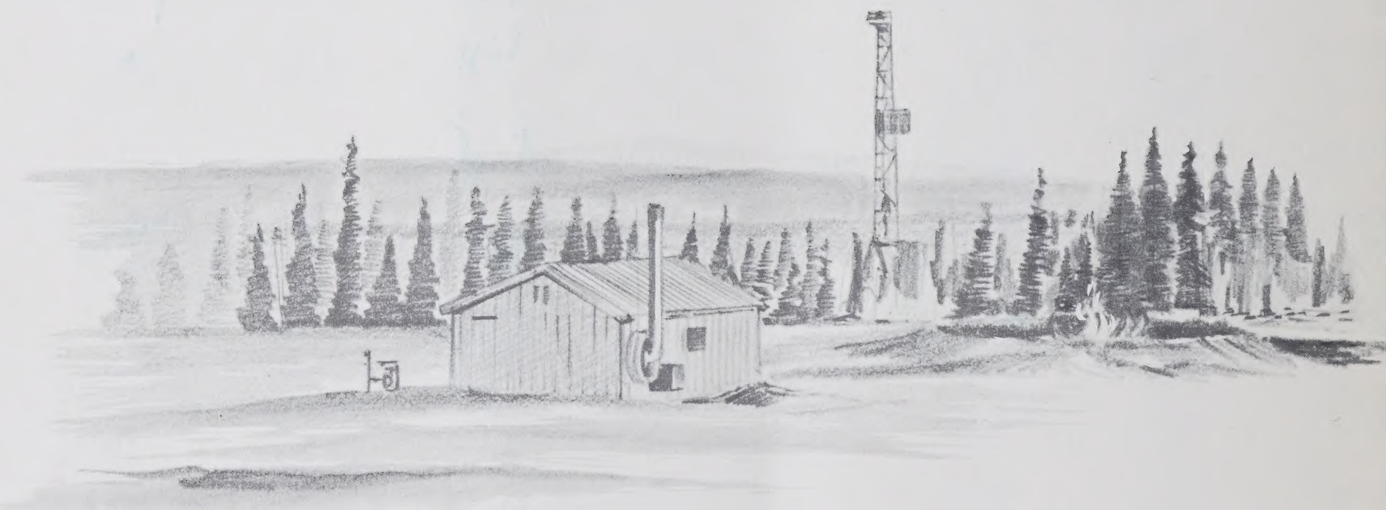
(1) The figures in this table are for Hudson's Bay Oil and Gas Company Limited and subsidiary companies at December 31, or for years then ended. With the exception of earnings per share, dollar figures are in thousands.

(2) Includes both capital and expense items; excludes interest and administrative expense.

OPERATING REVIEW (1)

1958	1957	1956	1955	1954	1953	1952	1951
19,395	20,963	18,040	11,091	5,413	3,526	2,303	2,078
1,316	3,073	2,359	(1,059)	(2,576)	(2,678)	(3,241)	(1,336)
.07	.17	—	—	—	—	—	—
2,472	4,742	2,245	729	—	265	—	—
3,788	7,815	4,604	(330)	(2,576)	(2,413)	(3,241)	(1,336)
12,480	15,155	1,632	(1,070)	(86)	485	1,358	670
4.2	5.8	1.3	.8	1.0	1.3	2.4	1.5
27,600	28,600	52,100	32,003	13,603	21,170	13,740	7,897
63,291	59,503	12,814	8,210	8,540	7,984	5,087	2,057
12,606	11,683	9,647	9,210	7,633	4,264	1,822	1,637
75,149	66,163	53,969	34,423	18,010	11,584	8,014	5,731
5,634	4,908	2,136	—	—	—	—	—
4,987	4,810	4,591	3,009	772	499	438	379
98,376	87,564	70,343	46,642	26,415	16,347	10,274	7,747
1,126	2,053	436	1,576	3,369	2,443	189	41
1,664	2,246	2,408	2,959	2,245	3,300	2,341	1,459
2,362	2,853	2,320	2,234	1,792	1,466	1,173	717
8,387	10,032	15,924	14,856	6,822	3,299	2,554	2,076
4,374	3,606	5,118	3,922	1,511	1,074	872	280
17,913	20,790	26,206	25,547	15,739	11,582	7,129	4,573
20,099	22,257	20,992	13,152	5,931	3,730	2,494	2,042
17,953	20,097	19,194	11,700	5,534	3,729	2,494	2,042
2,117	2,144	1,796	1,450	397	1	—	—
29	16	2	2	—	—	—	—
7,336	8,124	7,683	4,801	2,165	1,361	913	745
14.019	8.109	6.118	5.370	5.413	4.228	4.369	1.269
5.117	2.960	2.239	1.960	1.976	1.543	1.599	.463
192.0	184.0	335.0	318.0	166.0	134.0	91.0	48.0
102.2	107.7	186.2	174.0	81.7	55.3	39.6	27.3
71.9	74.8	153.4	156.6	56.5	38.7	19.4	6.8
55.8	65.4	149.2	154.1	55.9	34.9	17.8	5.6
9.3	5.1	.8	—	.4	.6	1.0	1.0
6.8	4.3	3.4	2.5	.2	3.2	.6	.2
30.3	32.9	32.8	17.4	25.2	16.6	20.2	20.5
2.0	3.6	6.6	5.5	5.2	.1	2.1	4.2
5.3	7.3	4.5	3.5	1.9	5.7	7.3	6.3
23.0	22.0	21.7	8.4	18.1	10.8	10.8	10.0
620.0	596.6	513.4	357.5	194.4	131.0	89.9	62.1
552.9	543.0	474.5	322.6	163.9	103.3	68.2	48.9
67.1	53.6	38.9	34.9	30.5	27.7	21.7	13.2
10,147	10,461	10,948	9,445	9,608	11,376	11,881	9,697
125	100	88	64	46	26	22	22
10,022	10,361	10,860	9,381	9,562	11,350	11,859	9,675
12,738	12,941	2	2	2	2	2	2
396	356	307	251	174	112	93	64

(3) The 1959 and 1958 figures have been restated to reflect a change in method, effective January 1, 1960, of calculating volumes accruing to royalty owners.



Lithokraft
OF CALGARY
LITHOGRAPHED IN CANADA